Testimony of the American Society of Travel Agents

The American Society of Travel Agents ("ASTA") is pleased to provide the Committee with the perspective of its travel agency members on the nature and extent of competition in the airline industry as it relates to the distribution system and on the impact of the Internet and, more specifically, the issues raised by the airlines' development of a joint Web-site to sell discounted fares to consumers.

ASTA was established in 1931 and is today the leading professional travel trade organization in the world. Its travel agency members account for more than half of the staffed, agency locations serving the public throughout the United States. ASTA's corporate purposes specifically include promoting and representing the views and interests of travel agents to all levels of government and industry, promoting professional and ethical conduct in the travel agency industry worldwide, and promoting consumer protection for the traveling public. ASTA has provided testimony to numerous legislative committees and fact finding bodies and has appeared in various legal proceedings; it is widely recognized as responsibly representing the interests of its members and the travel agency industry.[1]

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[1] See e.g. Investigation into the Competitive Marketing of Air Transportation, C.A.B. Docket 36595, aff'd; Republic Airlines, Inc. v. C.A.B., 756 F.2d 1304 (8th Cir. 1985); In re Domestic Air Transportation Antitrust Litigation, 148 F.R.D. 297, 61 USLW 2610, 1993-1 Trade Cas.(CCH) ¶70,165 (N.D.Ga., 1993); U.S. v. Airline Tariff Publishing Co., 1993-1 Trade Cas. (CCH) ¶70,191 (D.D.C., 1993); Spiro v. Delmar Travel Bureau, Inc., 591 N.Y.S.2d 237 (A.D. 3 Dept. 1992); and Crowder v. Kitagawa, 81 F.3d 1480 (9th Cir. 1996).

ASTA counts among its travel agency members about half of the so-called "traditional" or "brick and mortar" travel agencies in the United States, along with many of the pure on-line Internet agencies and hybrids, who together account for most of the sales of air travel, on and off the Internet, to the 230 million annual United States consumers of air transportation.[2]

Consumer Access to Information Issues: **The Orbitz Cartel**

When ASTA last appeared before this Committee, the focus of the hearing was on passenger rights, or the lack of them. Many bills were before the Committee, and other bills pending in the House of Representatives, dealing with airline competition in areas such as airline predation against new entrant competitors, slot allocations, perimeter rules at restricted airports, hub competition and other similar issues. Some of those issues have been resolved for the time being and others continue to deserve attention by the Congress and other federal authorities.

We told the Committee then, and believe even more strongly now, that failure to attend to the issues arising from the airlines' attempts to subvert the retail travel distribution system will make restoration and sustenance of meaningful airline competition impossible. We were then referring to the pattern of policies and practices adopted by most of the large airlines that are designed, and are having the effect, of making it more difficult for consumers to continue accessing the services of the only source of neutral, comparative price and service information, expertise and personal advice that exists – the travel agency

[2] Based on Travel Industry Association of America 1998 estimate of 221 million air person-trips taken in the United States, grown by 4 percent to 2000 annual estimated.

distribution system in all of its forms. Those practices continue unabated and have been supplemented with actions of the International Air Transport Association and the Airlines Reporting Corporation.

What we did not know then was that the airlines were preparing an "end game" maneuver designed to cut off the adaptation of the travel agency distribution system to the Internet while continuing to strangle the independent distributor with cost-increasing and business-interfering practices. We refer to the Internet Web-site known originally as T-2 and now officially named Orbitz. In its current form, based on the very small amount of information publicly available about it, Orbitz will be owned by five of the largest United States airlines, accounting for roughly 80 percent of all domestic air travel revenues. It boasts of providing "last minute web fares from the web sites of more than thirty airlines" on a "website like no other."[3]

In its earliest announcements, the founders claimed they would offer "the most comprehensive selection of on-line airfares and other travel information available anywhere on the World Wide Web," a site "superior to all travel sites," a site with "the best of everything."[4]

The airlines' use of the phrase "on-line airfares" does not refer merely to the publication on the Internet of otherwise generally available airfares. It refers instead to the publication of fares not available anywhere but the Internet, and thus leads to the additional

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[3] http://www.orbitz.com.

[4] Joint Press Release of United Delta, Northwest and Continental, November 9, 1999.

claim that “for the first time, on-line travel consumers will be able to compare and purchase the Internet fares offered by several airlines ... by visiting just one site.”[5] “It would support our business model if they supplied special Internet-only capacity.”[6]

In reality we believe the airline partners in Orbitz have agreed to arrangements for sharing fares and promotions that are designed to favor Orbitz over all other distribution outlets, on-line and off-line.

Whatever might be said about a fare-aggregation service by a neutral party in an industry with a clean antitrust record, there is reason to believe that the Orbitz project is in reality a collusive attempt by the major airlines to dominate the Internet space, and ultimately to displace the entire independent distribution system for the sale of air travel, through special arrangements to favor the Orbitz Web-site over all other independent Web-sites as regards the sale of “low fare” services.

Orbitz representatives have publicly conceded that the founding agreements for the Web joint venture provide that any carrier publishing a “lowest Internet-only fare” on its own Web-site must also provide that fare to Orbitz and may withhold it from all other distributors. In addition, we understand that the founding carriers and all of the so-called “charter associates,” comprising more than 30 airlines at this time, have agreed to provide various levels of in-kind promotional services for the site and that these commitments may

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[5] Id.

[6] Attributed to Ben Burnett, Vice President of Boston Consulting Group, a firm retained to act as “temporary launch manager.” “Nearly Two Dozen Airlines Will Join Planned Web Site of Four Big Carriers,” Susan Carey, Wall Street Journal, February, 2000.

be paid off by providing Orbitz with exclusive access to lowest Internet fare offerings. Total marketing support figures of $50 and $100 million have been mentioned. We're not certain of these details, of course, but if this is even remotely accurate, the inter-carrier arrangements for Orbitz are, in our view, unlawful as price fixing and as an exclusive dealing/horizontal group boycott of other distributors.

These arrangements, and likely others of which we are unaware at this time, give the lie to the position that Orbitz is "just another travel agency" scratching out a living in the dust, earning the same commissions and bearing the same costs as all other travel agencies. Orbitz says it is just a little agency with better technology, but this dispute is not about technology. It's about exclusive dealing reached through collusion designed to achieve market domination.

There are two alternative models of how the development of travel retailing on the Internet could proceed from this point forward. One is driven by consumer choices about how to research and buy travel. Airlines and other retail sellers would respond to those consumer demands by providing not only competitive air transportation services but competitive, efficient and innovative distribution services. In this model consumer preferences would dictate which retailer and which airline gets the business.

In the other model, airline decisions about how travel information should be parceled out would drive the outcome. The airlines would collectively dictate the channel choices for consumers.

As we said to the Department of Justice in our February complaint, the Orbitz arrangement appears to contravene the Department of Justice/Federal Trade Commission Antitrust Guidelines for Collaborations Among Competitors, in that it constitutes a marketing collaboration that

> involve[s] agreements on price, output or other competitively significant variables, or on the use of competitively significant assets, such as an extensive distribution network, that can result in anticompetitive harm. Such agreements can create or increase market power or facilitate its exercise by limiting independent decision making; by combining in the collaboration, or in certain participants, control over competitively significant assets or decisions about competitively significant variables that otherwise would be controlled independently; or by combining financial interests in ways that undermine incentives to compete independently.[7]

While the airline founders and other airline collaborators have pooled their money, there is no other apparent efficiency-enhancing asset integration involved that could overcome the anti-competitive implications of the “most favored agency” scheme that is the apparent heart of the deal. Moreover, as the Guidelines state:

> if the participants could achieve an equivalent or comparable efficiency-enhancing integration through practical, significantly less restrictive means, then the Agencies conclude that the agreement is not reasonably necessary [to achieve pro-competitive benefits].[8]

Why did United Airlines or one of the other founders not simply buy the software that Orbitz touts as the most significant innovation in travel since the jet engine and use it to compete against the other airlines? Why are the airlines once again approaching the marketplace

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[7] Antitrust Guidelines for Collaborations Among Competitors, April, 2000, at 14.

[8] Id. at 9.

as a unit rather than as the individual competitors that the Airline Deregulation Act envisioned? Why won't the airlines compete?

Orbitz is not alone. As the charts accompanying this testimony illustrate graphically, the world's airlines have been swift to copy the idea of the regionally based airline joint venture. Recent reports confirm that representatives of Orbitz have been in discussion with these nascent ventures regarding possible consolidation of operations into what would then be a global consortium of airlines jointly managing the dispersal and display of low-fare services to consumers worldwide. The charts show an industry with an overwhelming multitude of complex commercial relationships. See Exhibits 6 - 11.

Between the marketing alliances with antitrust immunity, the code sharing deals, the Internet joint ventures and cross-ownership arrangements involving airlines and Internet retailers, there is little left in which the airline owners of Orbitz are not involved in some kind of joint operation with the airlines that are supposed to be their arch-rivals. The Internet selling space is widely recognized as a growing long-term marketplace that can achieve for its participants unprecedented increases in efficiency, reach and content. If consumers want to go there, and many will, then all retailers should have a fair opportunity to reach them there with fully competitive offerings. The Orbitz plan is plainly designed to foreclose that possibility.

If successful in this effort, the airlines will enjoy an enormous economic windfall at the expense of the traveling public. Deprived of easy access to neutral, comparative information, the traveling public will, inevitably, make mistakes in air travel purchases, paying higher than necessary fares when there were cheaper alternatives and getting less optimum service for the travel dollars they spend. The ability of consumers to make optimal choices depends upon their having access to good information about the full array of choices available to them. That is the service that travel agencies have been providing so effectively since airline deregulation and which has led about 80 percent of the air traveling public to prefer agents as their source of information and travel documents. The Congress and other appropriate government agencies must act to prevent the airlines from monopolizing the distribution function.

For those reasons, ASTA urges immediate enactment of the portions of HR 2200, and the companion Senate bill introduced by Sen. Reid yesterday, that would make it unlawful for the airlines to offer differential fares to those persons favored with access to certain technology and would stop the airlines from continuing to operate free of the constraints of state consumer protection and tort laws. We also urge this Committee to communicate to the Department of Transportation that the review of the Computer Reservations System regulations, now years overdue, be given the highest priority. The anti-bias regulations should be applied to integrated Internet fare displays, and the rule allowing airlines to buy transaction information disclosing travel agency sales on competing airlines should be abolished.

It is not just against other Internet sites that the effects of the airlines' collaborative Orbitz effort must be judged. Orbitz is the intended coup de grace against traditional travel agents seeking a place in the Internet selling space. If successful in this strategy, the airlines would have Orbitz as the sole interface between the consumer and the carriers. The history of the airlines' treatment of travel agents, of all sorts, must be understood to appreciate the full potential consequences of the Orbitz venture, and how it serves as the final act in the airlines' script to deprive consumers of all other distribution system choices whether they are "bricks" or "clicks" or some combination.

As Alfred Kahn, the acknowledged "father" of airline deregulation, has observed, deregulation can continue "only in the presence of effective competition as the protector of consumers." Both economic theory and practice within the air transportation industry support the conclusion that the availability of comparative information about air transportation services is essential to vigorous competition among the airlines and necessary to the maintenance of affordable fares and responsive services throughout the country. Since 1978, the stated policy of the United States, as manifested in the Federal Aviation Act of 1958, amended by the Airline Deregulation Act of 1978, has been to promote aggressively conditions of competition between and among the airlines.

Travel agents provide two crucial services essential to assuring the competitive environment necessary for the public to benefit from, rather than be victimized by, airline deregulation.

First, they facilitate entry, exit and price and service competition among existing and new entrant airlines. Agents provide every carrier, in every market, an instant professional distribution system ready and able to inform the public of service and price options and to sell all of the inventory available at any moment, with no additional investment required by the airlines.

Second, travel agents promote the use of air transportation services by the public by serving as the only one-stop, neutral source of comprehensive information and counseling about a complex, constantly changing array of fares and services.

Indeed, the unsurpassed efficiency and effectiveness of travel agents at the daunting task of gathering, sorting, analyzing, and providing advice with respect to the bewildering array of alternatives that make up today's air transportation options has been repeatedly demonstrated.

On its 9:00 p.m. e.s.t, January 19, 1998 broadcast of its "20/20" television news magazine program, ABC-TV presented a segment in which a travel agent was shown to consistently quote a lower fare for given city pairs, under identical conditions, than a reporter could obtain by calling the airlines. Co-host Hugh Downs summed up: "But a good rule of thumb is that a good travel agent can do better than you can."

The "20/20" segment confirmed the findings of an earlier, November, 1997, independent study from the U.S. Public Interest Research Group ("PIRG"), which, in turn, confirmed PIRG's previous 1996 study. In the PIRG study, on October 9 and 10, 1997, PIRG staff, students and volunteers telephoned 8 to 10 travel agents and as many as 5 airlines in each of 28 cities, to obtain quotes for the "lowest" airfares for specific round trips originating in that city. Full fares, 1-week advance and 3-week advance fares were obtained for the departure/return dates of: (1) Thursday, October 16/19, 1997 and (2) Thursday, November 6/9, 1997. All quotes included a Saturday night stay. Departures were requested around 5 p.m. and returns around 6 p.m. on both dates.

The PIRG callers expressed flexibility to depart from any airport serving a multiple airport city, and the willingness to make one stopover. Tickets were not booked, since booking tickets would have changed the pricing structure of that particular flight. The study found that the lowest fares were obtained more often from travel agents than from the airlines.

According to "The 1998 ASTA Consumer Travel Purchase Report," a study conducted for ASTA by Plog Research, Inc., air travelers place greater trust in travel agents than any other travel information source, and technology makes no comparable improvement in credibility for the most experienced travelers. Given the credibility achieved by travel agents, the Plog study concluded, it follows that travelers believe that the best way to insure that they get the travel products and services they desire is to use a travel agent when making air travel purchases.

Because they are already the public's overwhelming choice as a source for travel information and arrangement expertise, there is every reason to believe that travel agents can also deliver air transportation services more efficiently over the Internet and through other electronic systems than can major airlines. Nonetheless, major airlines appear determined to reduce or eliminate the role of travel agents and other independent distributors' in the information, sales and distribution process regardless of the medium.

During the early years of deregulation these functions of the professional full-service travel agency served the needs of the airlines very well. Once the airlines' ability to fix commissions by agreement was ended by the Civil Aeronautics Board, competitive forces led to the expected and inevitable rise in agency compensation to the level of 10 percent of the fare sold as a “base commission” for all transactions. Travel agencies made rapid competitive maneuvering possible in an environment where the race went to the swiftest. As the airlines adapted to the new competitive marketplace, they earned considerable profits during the 1980's. Deregulation thus produced benefits for the major airlines as well as the traveling public.

Travel agencies also benefitted. The public liked what travel agencies did for them, and they flocked to agencies for help with the morass of fares and schedule changes that deregulation produced as the necessary corollary to a free market. The market share of travel agencies for air transportation rose from a pre-deregulation level in the low 40 percent range to about 80 percent for domestic sales and over 90 percent for international business. Travel agencies account for more than $120 billion in travel sales annually, some seventy percent of which is air transportation.

Travel agencies continued to do well even when the fortunes of the airlines turned down in the early 1990's.[9] The airlines lost billions a year while agency sales continued to rise (save only for the Gulf War year of 1991).

More recently, with the consolidation of the industry into a handful of giant carriers, and with various other types of alliances being almost routinely approved by the government, these large airlines began to recognize new fundamentals of the competitive market that had evolved. First, they saw that travel agents were a potential obstacle to

[9]The agencies' share of airline sales rose from 55 percent in 1977 to 81 percent in 1995. P. Ruden, Competition in the Distribution of Travel Services 5 (ASTA 1997).

their long-term objectives: agents made sure that consumers fully understood all of the fare and service options open to them. Second, the airlines came to understand that consolidation of the airline industry, combined with the success of passenger loyalty programs, had yielded genuine market power for them as against the travel agencies and other independent distributors. Third, for the first time, an apparent alternative to distribution through travel agencies had emerged: the Internet, by which the airlines believed they could control directly the information provided to the public without meddlesome interference by travel agents telling a somewhat different, and unbiased, story.

The Airlines' Strategy

The airlines' determination to dominate the retail distribution of air travel has a long history:

> Prior to the development of a domestic industry travel agent program, the airlines individually used many methods of distributing their tickets to the general public. Tickets were given with almost no restrictions or controls to hotel porters, bell captains, bootblacks, taxidrivers, barbershop proprietors, and virtually anyone else the airlines felt had a chance to sell their product. The use of such non-professionals had the potential to, and did in fact, cause great disservice to the traveling public and the airlines. The [Civil Aeronautics] Board found that the situation "was unsatisfactory and often resulted in abuses and mistreatment of the traveling public." ATC Agency Resolution Investigation, 29 CAB 258, 288 (1959)....[10]

The solution developed was joint airline control of the entry and operating standards of travel agencies, accompanied by immunization of the airline agreements from application

[10] Initial Decision of Administrative Law Judge Ronnie A. Yoder, Investigation into the Competitive Marketing of Air Transportation, CAB Docket 36595, served June 1, 1982 at 44, n. 3, final decision in Order 82-12-85, December 16, 1982.

of the antitrust laws pursuant to special provisions of the Federal Aviation Act. The airlines agreed to share the distributors, making the distributors agents at law and giving the airlines joint control over entry and joint power to terminate. The airlines proceeded with Draconian efficiency:

> A disapproved applicant ... receives no notice of the grounds for his rejection. Indeed, no record of the grounds for disapproval is made by the [ATC Agency] committee .... Agents who have been accredited may be removed from the agency list .... No formal notice of review is sent to the agent, who is granted no opportunity to present a defense to charges against him. If the vote is adverse to the agent, his name is deleted from the approved list and his agency agreement is terminated.[11]

The airlines also jointly set commissions for travel agencies, the agreements for which also received antitrust immunity until shortly before the deregulation of the airlines. When deregulation became national policy, the Civil Aeronautics Board withdrew antitrust immunity from commission setting and that practice stopped. The competitive market quickly led to an increase in commissions from the 1977 average of 8 percent to the 10 percent level that would persist until 1995. In the process of deregulating the airlines, however, the Congress conferred upon the airlines a privilege almost as valuable as antitrust immunity: the preemption of state laws “relating to” routes, rates and services of the airlines.

In the time between enactment of the Airline Deregulation Act and the official expiration of the Civil Aeronautics Board, the CAB re-examined the agency programs of both the domestic and foreign airlines. Here too, on the promise of “new forms of

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[11] ATC Agency Resolution Investigation, 28 CAB 258, 260 (1959), footnotes omitted.

distribution" emerging in a more open market, the CAB withdrew antitrust immunity from the agency programs. In the market chaos that followed airline deregulation, the travel agents' share of the air travel business increased to about 80 percent.

Despite many predictions to the contrary, "new forms of distribution" did not arise. Instead the airlines embraced a new method of controlling the agency distribution system that was now serving most of the industry's customers with information and transaction services. In the late 1970's the opposition of the Department of Justice, and other factors, had led to the collapse of industry plans to build a single computer system to provide fare and service information to the agency system. Instead, some airlines, led by United and American, started leasing their own "CRS" systems to travel agents. The flights and fares of non-owning airlines were included, to make the systems more attractive to travel agents each of whom continued to represent all airlines through blanket agency appointments conferred through the Airlines Reporting Corporation and the International Airlines Travel Agency Network.[12] Some airlines became "co-hosts" with the system owners, and it soon became apparent that the airline owners who controlled the information were biasing the computer displays to favor themselves at the expense of non-owner airlines. The Civil Aeronautics Board was forced to adopt comprehensive regulations to control the airline CRS-owners' desire to prejudice downstream air transportation and subordinate the agency distributors trying to provide unbiased information to the public.

[12] These programs were originally administered by the airlines' trade associations. They were spun off into separate companies owned directly by the airlines when the CAB terminated antitrust immunity.

Those regulations remain in place and yet another five-year review of them is currently pending at the Department of Transportation.

In the early 1990's a new development occurred that heralded things to come. A number of major airlines were sued in a class action in Atlanta, alleging, among other things, that the airlines were using their CRS systems to signal each other regarding plans to increase prices. These signals, it was claimed, were used to reach consensus on price increases and to threaten or discipline carriers that stepped out of line. The case was eventually settled through the provision of coupons to class members, which coupons were good for a discount on future transportation on the defendant airlines.

The settlement agreement, hammered out behind closed doors, provided that the coupons could not be redeemed by travel agents. If allowed to proceed, this deal would have deprived travel agents of revenue on some $450 million in business and forced their clients to deal directly with the airlines to “benefit” from the coupons. When ASTA complained to the court that the settlement agreement had been used to produce a brand new antitrust violation, namely a horizontal group boycott of travel agents by the defendant airlines, the airlines withdrew that portion of the settlement. When the Department of Justice brought the same allegations against the airlines in Washington, they settled that case too.

As Internet technology emerged in the early 1990's the airlines were relatively slow to move. Independent firms entered this new arena first and most aggressively. Firms such as Travelocity, Expedia and others established name recognition nationally. Having seen a new tool that attracted considerable public attention and patronage in a short period of time, the airlines began a program of reducing travel agency compensation, as reflected in Exhibits 4 and 5 to this statement. While telling travel agencies that they could make up some of the revenue loss by charging the public fees for the agencies' services, the airlines refused to consider changes to ticket documents that would facilitate agents' doing that in the most efficient and customer-friendly way.

At the same time traditional travel agencies also saw that the future of travel retailing was, in part at least, going to be a Web-based process and that they needed to move to that space as well. In the late 1970's CRS systems had made it possible for the smallest travel agency to replicate the inventory available to even the largest retailers and thereby give consumers a full set of choices as well as expert advice. Now in the 1990's the Internet offered the smallest agency the opportunity to expand its market reach across the country, and even across the globe, while achieving new efficiencies in communication and research.

While most of the attention is paid the largest on-line agencies, ASTA's members, most of which are dwarfed by firms like Travelocity and Expedia, are moving rapidly to the Web. Our most recent survey data shows that fully half have their own Web-sites. These do not begin to rival those of the major players in scope and sophistication, but they represent a crucially important presence in this marketplace and, absent interference from the airlines, they will continue to grow in number and complexity. Most of these Web-sites represent the integration or "convergence" of Internet technology with more traditional methods of retailing and are the model of business most typically to be followed by smaller firms seeking niche positions in the Web-based market rather than trying to go head-to-head with larger firms who entered the market earlier.

Agency on-line air sales are estimated to reach 5 percent of total U.S. airline sales in the year 2000 (see Exhibits 1, 2 & 3), slightly ahead of the airlines' aggregate performance in the absence of Orbitz. Most importantly, the current annual growth in retail sales of air travel, driven by a strong economy and high employment, is going to the Internet. Firms not participating in "Internet sales," are both fewer in number and living on a shrinking volume of business despite growth in the overall market.

The airlines were swift to react to agency incursion into the Internet selling space. To name but a few steps taken, the airlines imposed differential commission levels on Internet-originating transactions and, working jointly through the Airlines Reporting Corporation, imposed new identification requirements on Internet-originating tickets to identify those transactions to which the lower commission levels would be applied. They have jointly posted a list of recommended and actual practices that discriminate against on-line transactions.

Here we must emphasize that while some people, including those at Orbitz, have argued that the current dispute about the joint airline Web-site is really a fight by the two dominant on-line agency firms, Travelocity and Expedia, to protect themselves from competition, the reality is that there are thousands of smaller travel agencies that want to use the technology of the Internet to expand and grow their businesses. More importantly, millions of consumers prefer the "traditional" travel agency as the source of information, advice and travel documents either alone or in combination with Internet capabilities. And, of course, there are millions of Americans who do not have realistic and practical access to the Internet and who, if they are to take advantage of travel, must be able to find and access a so-called “traditional” travel agency.

The story is not over. When the airlines were called to account for rising customer dissatisfaction with the way they are treated, the airlines, under threat of action by this Committee and others in Congress, sought the equivalent of a “plea bargain.” They produced the “voluntary” service commitment program which was the subject of interim review by this Committee just a few weeks ago. Again, given the opportunity to collude and get an agreed-upon price advantage over the retail distribution system, they did so, this time by providing that the lowest fare guarantee in their service commitment applied only to customers choosing to deal directly with their reservations centers. Customer using travel agents, on-line or off-line, were excluded from this benefit. The same was true for the grace periods provided for holding fare quotes for 24 hours while searching for a better fare elsewhere. It was Atlanta all over again.

The repetitive nature of this joint conduct by the airlines establishes a clear pattern. They now intend to block agent access to the lowest fares and raise agents’ costs of doing business while continuing to lower their compensation and interfere with their customer relationships.

Armed with motive and opportunity, the airlines have now embarked on a campaign to reshape the market in their own image. If successfully consummated, this strategy will make it much harder for the public to learn about all of the fare and service options available to them and thus increase the likelihood that they will, on the whole, spend more for air travel than they otherwise would. By restricting access to unbiased and comprehensive information from independent sources, the airlines expect, rightfully, that they will be able to increase the average price consumers pay for air travel.

Travel agency sales of air travel alone exceed $80 billion annually. If the airlines can divert any meaningful amount of this business to themselves, the potential gain to them is enormous, not merely in commissions avoided, but in the higher overall prices that consumers will pay for air travel. Deprived of easy access to independent sources of comparative price and service information, consumers inevitably will end up paying more, on average, even if the airlines never actually raised another fare.

The changes the airlines are aiming at the distribution system are not occurring under conditions of a level competitive playing field in which consumer preferences ultimately control the outcome. Instead, the airlines are using market power, collective activities and other devices to undermine the distribution system to achieve their goal of reducing the public's access to independent comparative price and service information.

The airlines have reduced both off-line and on-line commission rates to levels that do not cover agency costs. This has forced most agencies to charge their own fees to consumers for the sale of airline tickets. Agency tickets sold on the Internet have been singled out for even lower commissions. Enforcement of those discriminations is aided and abetted by the airline-owned Airlines Reporting Corporation. The carriers also enforce brutally discriminatory ticketing policies on travel agents while disregarding those same policies in their direct dealing with consumers.

The airlines jointly have refused to permit travel agency service fees to be placed on the airline ticket stock, thus denying agents an important adaptive efficiency, while they continued for many years to apply self-serving discriminatory compensation policies to their jointly owned sales agency for government and large corporate clients.[13] Finally, they continue, under authority approved by the DOT's CRS regulations, to share detailed information on their competitors' sales to consumers. Details of these activities are set out in Appendix A to this Statement.

Consumers must have access to travel agents and other independent distributors who provide unbiased consolidated schedule and fare information if we are to preserve competition in the airline industry and maintain a system that provides the public with a broad range of options, including access to small airlines and start-up carriers.

Since deregulation, the public has had the choice of buying directly from suppliers such as airlines at no additional cost and overwhelmingly has chosen to deal with travel agencies. Consumers prefer dealing with travel agencies rather than airlines when purchasing air transportation because agencies deliver far more value, convenience and services.

Among the most basic functions performed by travel agencies is to collect and distribute comparative information and advice about the price and quality of travel

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[13] SATO was later sold to non-airline interests. See Appendix A.

suppliers' offerings — a function that no single airline can or wants to perform. In addition, consumers' transaction costs are often lower than direct-dealing with airlines, especially because many travel arrangements are joint purchases of the products of several travel suppliers (for example, air transportation and hotel/rental car). In short, one-stop shopping for accurate and unbiased travel services at a travel agency is the essence of the benefit to the public, as against airlines' direct selling methods.

It can no longer be assumed, that, even with new technologies, travel agencies will be able to function in the future as independent sources of the services that consumers value. Slowly but surely, in a myriad of ways including those we have identified above, and in cumulative effect, the major U.S. airlines are destroying the competitiveness of travel agencies and, thereby, extracting ever-higher effective prices for air travel from consumers.

In lock-step, each of the major carriers (American, Delta, Northwest/Continental and United) that comprise the U.S. airline oligopoly, has imposed virtually identical restraints upon independent travel agencies, for the purpose and having the effect of, depriving consumers of the benefits of free and open competition. Specifically, the restraints we have identified, are designed to impede and prevent travel agencies from offering a full range of consumer services and thereby cause travel purchasers to by-pass agencies in favor of direct-dealing with carriers.

The ultimate objective and actual effect of this strategy is to warp the normal discipline of the market place and enable each airline to achieve more than competitive profits by exploiting consumers' inability to search out and obtain the lowest possible ticket prices. In other words, these restraints make possible an adverse impact upon consumer welfare much like that one would expect from traditional cartel behavior.

No airline can be expected to provide the public with unbiased comparative price and service information about its competitors. Consumers may be able to get some of this information from airline-controlled Internet sites, but the fundamental airline strategy of disabling the travel agency distribution system will leave millions of consumers without effective access to neutral comparative information.

The latest airline attempt to deprive the public of its only opportunity to leverage what little competition there is must be stopped. At the same time, the unbalanced conditions that encourage the airlines to try every avenue to deprive the public of its only neutral, unbiased source of travel information and arrangements must be returned to equilibrium.

There are important areas of government action available, short of re-regulation of the airline industry, that would go a long way toward restoring the balance of power and assuring that consumers are not left to the airlines' dictation of distribution channels.

One step is to pass the portions of HR 2200 that would make it an unfair practice under the Federal Aviation Act for any airline to make the availability of a low fare dependent upon the technology used to access information about the fare. This one step would assure that the millions of Americans lacking effective access to the Internet are not deprived of access to the lowest fares and it would assure all Americans of the freedom of choice as to distribution channel with which to do business. Airlines could continue to offer low fares and consumers would decide how to research them and how to buy them.

Another step, also fundamental, is to fix the problem of federal preemption of state law. When Congress deregulated the airline industry by passage of the Airline Deregulation Act of 1978, it prohibited states from "enact[ing] or enforc[ing] any law *** relating to rates, routes, or services." 49 U.S.C. App. § 1305(a)(1). Obviously, such a provision was necessary to prevent the states from subjecting to their regulation that which Congress had just removed from federal regulation. That federal preemption provision, shielding airlines from state regulation, has now been turned by the airlines into a sword with which they bar the general public and small businesses from holding them accountable under the same state law that applies to virtually every other industry in the country. The result is that the airlines have become a veritable law unto themselves, immune from state-law suits seeking to hold them responsible for harm to passengers as well as their obligations to small businesses. At the same time, the airlines remain free to call upon, and do call upon, these same state law principles against other parties when their own interests are served.

Differences of interpretation in the scope of the Federal preemption that several Justices of the Supreme Court would accord airlines under the Airline Deregulation Act, as well as instances of members of the public and small businesses, including other airlines, being denied a forum for their claims, illustrate clearly that clarification and modification of this troublesome provision must be undertaken.

Absent a comprehensive and active administrative scheme for dealing with private party grievances, there is simply no place to go to get justice from an airline. The Department of Transportation "has neither the authority nor the apparatus required to superintend a contract dispute resolution regime."[14] Clearly, it is unequipped to resolve tort claims.

ASTA supports statutory language it believes strikes the appropriate balance between the airlines' need to be free of state economic regulation of fares and routes in a deregulated environment, and the rights of consumers and others to have redress against airlines for their failures to abide by the same state law standards of conduct all other parties must observe. That language amends 49 U.S.C. Section 41713(b) by providing:

> **This subsection shall not bar any cause of action brought against an air carrier by one or more private parties seeking to enforce any right under the common law of any State or under any State statute, other than a statute purporting to directly prescribe fares, routes, or levels of air transportation service.**

This language currently appears as Section 3 of HR 2200, and also in Section 7 of S. 477, the "Airline Competition Act of 1999," offered by Senator Schumer, and as Section 9 of H.R. 272, the "Airline Competition and Lower Fares Act," offered by Representative Slaughter.

Finally, if the government allows the airlines to proceed with Orbitz as planned, it will have done at least three things: (1) defeated completely the goals of the Airline Deregulation Act of 1978, (2) rung the death knell of many small businesses throughout

[14] American Airlines, Inc. v. Wolens, 513 U.S. 219, 232.

the United States who will have no effective means of competing with collusive airline distribution systems, and (3) left consumers with no long-term hope of relief from the anti-competitive behavior of the airline industry.

In such circumstances, where the airlines will for all practical purposes be a single enterprise (when effect is given to all the other relationships, immunizations and preemptions that the law and regulators have provided them), it will be essential to permit the distribution system to join together in collective action, with similar relief from the antitrust laws, in dealings with the airlines. If the United States air transportation system is to be run by an unregulated cartel, elemental fairness, not to mention the welfare of the millions of consumers who prefer not to deal directly with the airlines, requires that travel agencies and other distributors of retail air services be allowed to collectively bargain as a union would. Absent such relief there would be no semblance of fairness or competitiveness in the marketplace that the airline industry of three or four carriers would produce.

Conclusion

Independent providers of travel services are absolutely necessary for optimal consumer welfare. Consumers derive substantial benefits from the presence of travel agents in the travel service market. This is as true of the Internet as of the more traditional selling space, maybe more so.

Both economic theory and recent history teach a clear and important lesson: the firms that comprise the U.S. airline oligopoly are prone to anti-competitive acts of predation and collusion.[15] Their past conduct demands constant and heightened scrutiny of their practices toward travel agencies.

The acts and practices we have discussed threaten permanent injury to the competitive process and, unchecked, will result in the transfer to the major carriers of vast amounts of wealth that consumers would otherwise enjoy. These and other carrier-imposed restraints deny to travel agencies the freedom to take independent actions that would make their operations more efficient and responsive to consumer demand.

By restricting travel agency output, these restraints also enable individual carriers to exercise power over price in discrete geographic markets for air transportation. Taken together, their aggregate effect is to allow carriers collectively to overcharge consumers on the order of hundreds of millions of dollars more annually than they could earn under fully competitive conditions— a rate of welfare loss that will only increase over time unless the carriers' anti-competitive conduct is stopped.

By restraining the competitiveness of an industry segment that serves all travel suppliers, not just airlines, the long-run welfare loss is even more severe than the loss extracted by a single monopolist that overcharges customers by setting price above its marginal costs.

At its core, and as a whole, the carriers' anti-competitive strategy is designed to erode the ability and incentives of consumers to seek and obtain the services of travel agencies, including emergent on-line booking services and auction sites. The airlines

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[15] See for example, U.S. v. Airline Tariff Publishing Co., 1993-1 Trade Cas. (CCH) ¶70,191 (D.D.C., 1993).

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Appendix A

Non-compensatory Commission Policies

The first action in the airlines' anti-consumer campaign began in 1995, when the major airlines, save only Southwest Airlines, capped travel agency commissions at $50 per round-trip ticket.   This was followed in September, 1997, with across-the-board reductions in the domestic base commission rate from 10 percent to 8 percent. In 1998 international commissions were capped at $100 per round-trip and in October, 1999, a third domestic reduction, to five percent capped, was imposed.[16] In dollar terms, the total compensation reduction to agents is well over 30%.[17]

At this time, consumers have overwhelmingly elected to continue to do business with travel agents, but millions of consumers now pay transactions fees to agents, fees which agents have been forced to adopt to off-set airline commission cuts. Consumers who are unwilling or unable to pay travel agent transaction fees must contact airlines directly and often pay higher fares as a result. As airlines continue to reduce agency commissions, many consumers may be willing to pay higher fees for the right to do business with agents, but millions of other consumers will be forced to deal directly with major airlines.

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[16] The last three reductions were all led by United, the lead investor in Orbitz.

[17] The commission rate for June, 2000 domestic air transactions was 4.10 percent according to official Airlines Reporting Corporation reports. In January, 1995, before the commission caps, the rate was 10.01 percent.

This puts the consumer right where the airlines want him, bereft of a neutral source of information to deal with a bewildering array of complex air fares and services. As travel agents are forced out of the industry and airlines secure more direct consumer business, consumer alternatives will continue to decrease resulting in significantly higher consumer travel costs. This “revenue squeeze” has made entire segments of airline ticketing activity non-remunerative for agents, a major factor in the exit of 18 percent of independent U.S. travel agencies from the air retail industry during 1995-2000,[18] as well as in a shifting of resources by the remaining agencies to non-air sales. This is the first decrease in the number of travel agencies since World War II, and more closings are expected as agency operating reserves are exhausted.[19]

Small domestic airlines, many international airlines, and start- up airlines who depend upon the travel agency distribution system will be adversely impacted if not eliminated. There is no alternate distribution system available to these types of airlines.

Major airlines have generally misrepresented the reason for agency commission cuts, citing a need to reduce expenses and pass savings on to consumers. In fact, airline ticket prices have steadily increased, and airlines are regularly posting record profits. Not one penny of the alleged cost savings can be discerned to have been passed on to consumers through better service or lower ticket prices. There have been no consumer benefits, and consumers are paying the highest airfares in history.

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[18] Between March, 1995, the first full month after the first commission caps, and March, 2000, the number of agency firms accredited by ARC declined from 23,978 to 19, 739. Source: ARC Monthly Statistical Information.

[19] Later ARC reports confirm this. Year-to-date terminations of defaulted agencies were up 39 percent at the end of June, 2000.

Agency Transactions Originating On The Internet

Major airlines have also adopted discriminatory and non-compensatory commission policies for bookings originated on-line.

Commissions paid to on-line travel agencies and other independent on-line ticketing services are at a general rate of 5 percent with a $10 maximum, which is well below these firms' costs. The airlines have thereby succeeded in arresting in its incipiency an effective counter-measure available to agencies to offset reductions in commissions on traditional sales: unfettered access to consumers through high-volume, low-cost electronic marketing systems.

Most recently, in implementation of the airlines' non-compensatory Internet transaction policies, their jointly owned alter ego, Airlines Reporting Corporation ("ARC") has begun issuing special numbers called Electronic Reservations System Provider numbers ("ERSP" numbers). Virtually all the major airlines have informed travel agents that they must attach these special numbers to every transaction that originates on the Internet. The only apparent purpose for this requirement is to help the airline enforce its discriminatory commission policy with regard to Internet transactions.

In this scenario, the airlines, through ARC, are collectively facilitating the enforcement of commission policies designed to keep travel agents from becoming meaningful participants in the electronic marketplace.

New Entrant Obstacles

For at least the second time since airlines were deregulated, the so-called “new entrant” airline group, which typically operates on a no-frills, low-cost, and thus low fare, economic model, is finding it difficult, often fatally so, to compete with major established airlines. Major airlines monopolize airport facilities, earn huge returns from the computer reservations systems they control and own (and through which almost all airline reservations are made), target small carriers using massive giveaways (such as frequent flyer program points), and employ temporary fare-cutting tactics to deter or block new market entry.

A competitive market for travel services, i.e., one in which consumers anywhere in the U.S. can readily turn to independent agents to reduce search costs and avoid buying errors, makes it possible for new carriers to enter the market and for small carriers to expand without bearing the full costs of second-stage entry (developing their own distribution network). Thus, carrier practices that restrain the ability of agents to compete also tend to raise entry barriers in air transportation markets. Federal agencies such as DOJ and DOT have long been concerned about market conditions that impede entry and expansion of small, low-price carriers, and there is good reason to believe that erosion of travel agency competitiveness will translate directly into less competition in the market for air transportation.

Moreover, market imperfections, including consumers’ notorious lack of information about carriers’ complex, ever-changing and often poorly visible price and service offerings, enable carriers with market power over particular routes and facilities to discriminate against captive consumers. By restricting travel agencies' output, individual airlines can and do exercise and maintain market power in discrete geographic markets for air transportation, especially city-pairs involving a "hub" where the carrier is the dominant or monopoly provider.

If the major airlines are successful in destroying most or all of the smaller, new entrant airlines, competition in airline pricing and schedules will diminish even further.

Discriminatory Ticketing Policies

Major airlines refuse to permit agents to offer certain benefits and concessions to consumers, such as the refund of so-called "non-refundable" tickets, while reserving to themselves the right to make such refunds. Transgressions are punished severely with airlines levying cash penalties against agents to which agents are summarily required to acquiesce or face the greater penalty of losing their ability to issue tickets altogether. The airlines themselves often issue such refunds. The airlines then typically force the agent to repay the commission earned on the original sale.

Similar discrimination in competitive practices occurs with respect to price-saving opportunities such as the sale of "back-to-back" and "hidden city" tickets, as well as highly publicized special fares that require consumers to purchase directly from airlines. These discriminations have the consequence of interfering with the relationship between the travel agency and its clients, by, among other things, impairing the agency's credibility in the eyes of the customer.

"Back-to-back" tickets, are a pair of tickets issued to permit the traveler to avoid the Saturday night layover normally required to get a discounted ticket. Airlines prohibit agents from issuing these tickets, and normally demand the agent pay the full coach fare as the penalty for so doing.

“Hidden city” tickets, in which the passenger buys a ticket A-B-C, which is cheaper than a non-stop A-B ticket, then gets off the plane at B, are also forbidden and punished severely. In addition, major airlines, while acknowledging passenger contracts for passage legally exist only between passengers and airlines, nonetheless reserve the right to penalize travel agents financially when consumers buy inexpensive round-trip tickets, travel one-way, and throw away the return portion of the ticket. Such policies confuse and anger the public, while undermining the relationship between the travel agent and his client, who expects the agent to find and ticket the lowest fare available.

Airlines have also adopted an identical condition upon redemption of frequent flyer awards that arbitrarily forces consumers to by-pass agencies. These awards are mostly earned at employer expense but are commonly used by individual travelers for leisure trips, many of which would have been arranged through travel agencies. The airlines divert substantial revenue from agencies by requiring awards to be redeemed directly from airlines.

As recently as January 11, 1999, Delta Air Lines announced initiation of a $1 surcharge for each published fare component on all U.S. domestic fares. Under this scheme most round-trip tickets, which are constructed using two fare components, would include a $2 surcharge. Additional surcharges would apply on tickets constructed using multiple fare components. This surcharge, however, would not be applied to tickets issued via Delta’s SkyLinks Internet web site.

Thus, Delta's scheme penalized all of its customers who wished to avail themselves of the opportunity to receive comparative cost data by consulting a travel agent. The avoidance of the $1 surcharge penalty by using the Delta web site was "fool's gold" placed in consumers' paths to lure them into remaining in the dark about fare alternatives that could potentially save them hundreds of dollars.

Delta cited increased computer reservation system ("CRS") booking fees as its justification for this punitive charge for using a travel agent. Since the airlines by and large own the CRS systems, they are both responsible for, and benefit directly from, the increased CRS booking fees of which Delta complained.

In this case, at least, the public outcry was so great that the other airlines declined to match the Delta surcharge. It was dropped after a few weeks. Delta nonetheless stated that any passenger seeking to get credit for having paid the $1 surcharge would have to pay a $75 change fee that Delta imposes on discount tickets.

Airlines Use of Joint Assets

The airlines also use discriminatory collective or joint operation of assets to offer concessions, benefits and services to the public while denying comparable access to such concessions, benefits and services through travel agents and other independent air transportation distributors, including, but not limited to, joint sales activities, denial of competitive tools, and denial of distribution efficiencies. The airlines operate several collective businesses that are used to disadvantage travel agents and to limit public access to comparative price and service information.

These include ARC, which controls both who can become a travel agent and the settlement of funds between travel agents and the airlines. ARC is also involved in the formatting of standard agents' ticket stock. When the airlines cut commissions in 1997, the travel agency community sought the inclusion on the ticket document of a space where the agent could insert its own service fee and process the charge through ARC along with fares, taxes, and other charges on the ticket. The airlines have made it clear that this important competitive efficiency mechanism will not be provided to travel agents.

More recently ARC has begun providing "accreditation" of corporate customers, purporting to make them "agents" of the airlines that sell to them, so that the corporations can have standard travel agents' ticket stock and settle accounts with the airlines through the same system used for travel agents. In purpose and effect, this program is collective action that facilitates the carriers' strategy. Among other things, it enables them jointly to target, select, large volume corporate accounts that constitute a large and lucrative source of agency profitability and skim the "cream"[20] for themselves.

Another example, until recently, was the operation of SATO, Inc., the functional equivalent of a mega-sized travel agency (air sales of about $1 billion) that the airlines collectively owned and used to compete with travel agencies for government and corporate

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[20] As Justice Brennan, observed, concurring in White Motor Co. v. U.S., 372 U.S. 253 (1963):

> Instead, [defendant] seeks the best of both worlds— to retain a distribution system for the general run of its customers, while skimming off the cream of the trade for its own direct sales. That, it seems to me, the antitrust laws would not permit...

business.[21] The airlines claimed that SATO was more cost-effective than travel agencies and was operated on a non-profit, strict cost-pass-through basis, but there was evidence that the actual cost of SATO on a percentage-of-ticket-price basis was several points higher than the average actual cost of travel agency commissions. And when the airlines capped travel agent commissions, no reduction was placed on SATO's working "commission," thus increasing the advantages it had over regular travel agencies.

In fact, exempt from the same commission caps and ticketing restrictions that the carriers have imposed upon travel agencies, SATO enjoyed an effective commission rate of approximately eleven (11) percent, almost twice as much as agencies' average gross commissions on air sales. SATO has now been sold, but its historical collective use as an unfair competitive weapon against travel agencies remains a fact.

Agents' Transaction Data

One of the most egregious of the airline practices in question, is the process whereby the airlines share competitively significant sales transaction data in violation of the confidentiality interests of the travel agents and other independent air travel distributors who generated the transactions.

Confidential business information generated by travel agencies is routinely captured and shared by the airlines in a manner that would be blatantly unlawful absent regulations issued by the Department of Transportation. Those regulations require each

[21] Since this paper was first written, the airlines have announced that SATO, Inc. has been sold to private investors who will operate it as a travel agency. We do not know at this time with certainty whether a special relationship between SATO and the airlines will survive this sale.

computer reservations system (most of which are controlled by airlines) to make available to all participating U.S. airlines all marketing, booking and sales data that it generates from its systems.

In addition, ARC sells to airlines travel agency "total sales" figures, information that would normally be confidential unless a business consented to its disclosure. Because airlines are major competitors of travel agencies, there are serious questions as to whether they should have access to proprietary data of this kind.

If competitors in any other industry were to sit around a table and exchange this type of information in the ordinary course of business, we believe that the Department of Justice would lower the antitrust boom on them. Yet the airlines are free to share competitive information about their operations with their competitors without apparent concern. And the information is then used to disadvantage the travel agency, the only independent source the public has for neutral, comparative information.